

Retention Attention

Leasing experts employ creative strategies to keep properties occupied.



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What do leasing reps have to do these days to fill their spaces? Well, what about bartering? "It's something we are working out," says **Stan Stouder, CCIM, a partner with CB Richard Ellis Brokerage Services in Fort Myers, Fla.** "We are working with vendors who do lawn maintenance, asphalt seal coating, tree trimming. If they provide a service we consume, we are willing to exchange their service for rent. We may turn one of our vacant buildings into an incubator building for these and other small users."

All over the country and in all property sectors, commercial real estate professionals are thinking outside of the box to find ways to cope with today's economic conditions. In particular, leasing experts involved with all property types are exploring the best ways to maintain occupancy and property value while granting tenants more control and flexibility, from reducing rent to offering incentives.

A Taxing Situation

"What seemed negative - a major tenant downsizing - ended up having a positive outcome for both parties," says **Lauri L. Greenblatt, CCIM, CPM, president and principal of Promus Management in San Diego.** A long-term primary tenant - an educational nonprofit organization - recently approached Promus for help with leasing its 9,000-square-foot space in a 17,000-sf office building. "The tenant requested rent relief and threatened to exercise its cancellation process if help wasn't forthcoming," Greenblatt says.

However, "a face-to-face meeting with its chief executive officer revealed that the tenant didn't actually want to move but had lost more than 10 percent of its revenues and laid off staff due to recent government budget cuts," Greenblatt says. The situation called for a creative strategy, "and, due to the tenant's nonprofit status, we were able to craft a win-win solution."

"As part of an overall repositioning of the building, we negotiated a new lease, shifting the responsibility for property taxes to the tenant," Greenblatt says. Because of its nonprofit status, the tenant was able to apply to the county for a property tax waiver. "We also agreed to take back about 20 percent of the tenant's space in return for a two-and-a-half year extension on the lease and a slightly higher per sf rental rate."

As a result, Promus helped the tenant "reduce its total cash outflow by 13 percent and give back excess space," Greenblatt adds. Promus now can "reduce its exposure by adding multiple tenants and increase its cash flow by 12 percent over the previous lease when the spaces are leased." This extra cash flow should pay back re-tenanting costs within six months, adding close to \$1 million in value to the property, Greenblatt adds.

Industrial Park Provides Incentives

Until 1007, Metro Distribution Center, a 263,400-sf industrial park in Fort Myers, Fla., was running at 90 percent occupancy. Today, the park is 50 percent occupied with future lease expirations and tenant defaults possible. It's also carrying three empty 10,000-sf buildings.

"In 2007, one tenant's business dropped precipitously, yet he faithfully paid his rent until his lease expired," says **Stan Stouder, CCIM, partner with CB Richard Ellis in Fort Myers.** Instead of losing the tenant, Stouder figured out a way to help it stay put.

"While the tenant ended up retiring, we initially offered to let him stay for 12 months and just pay common area and maintenance fees, real estate taxes, and insurance," Stouder says. Under this arrangement, the tenant's base rent of \$60,000 for 2010 would be completely abated. And since the center had vacancy, if a prospective tenant sought the space, "I would ask [the existing tenant] to move to another 10,000-sf building in the park."

Stouder employed this tactic because he believes it's important to reward tenants who are keeping their commitments. In addition, "getting reimbursed for my expenses is better than having an empty building," he says.

To market the park's empty buildings, Stouder has created several strategies to entice new tenants. First, he has made the buildings as aesthetically

pleasing as possible, including repainting everything from the buildings to fire hydrants, straightening fences, cleaning windows, and sprucing up the grounds, he says. He has lowered the base rent from \$5.95 psf to \$4.95 psf and offers free rent for financially qualified tenants. In some cases, he will "do tenant improvements at no charge to qualified tenants and provide rent credits for TI expenses they incur if the improvement has potential for subsequent users," he explains.

Keeping the Life in Lifestyle Center

"The key is to help tenants who have a solid business and would be doing well if not for the current economy," says **Beau Beery, CCIM, director of commercial brokerage and asset management for AMJ of Gainesville, Fla.** Knowing that tenants will thrive when the market turns around, "it is beneficial to try to keep them in place." This is what drove Beery to help out several tenants in one of his company's 90,000-sf lifestyle centers.

"We have been approached by a number of tenants, both national and local, needing help in this down market," Beery says. Five of the 20 current tenants in the center have asked for help, with one tenant leaving, he says. "Out of the four tenants we are helping, three are rent freezes, and one is a rent reduction."

The first step is to review tenants' financials before making any decisions. "Tenants know that there needs to be a justification for their request and this has to be in the form of reviewing their personal and business financials. Those financials must tell a story of need," Beery says.

Once the tenant has been approved, "the difference between what their rent should have been and the new 'help' rent is now money they owe in the form of a note amortized over a negotiated period following the help year," Beery says. AMJ also is willing to lower a tenant's rent for one year in exchange for percentage rent so that when the market bounces back, Beery and his colleagues are rewarded for taking a chance on the tenant.

But even before the market bounces back, landlords can reap several benefits from lowering or freezing rental rates. For example, it can "save on replacement costs, lead to a strong tenant-landlord bond, increase the tenant's renewal likelihood, increase the property's overall value in the event of a sale, create synergy among the other tenants, and help stop the exercise of co-tenancy clauses," Beery says. "As landlords, it is a balancing act between giving tenants just enough help to survive a storm and giving them too much of a discount for too long, hurting the property's value," he adds.

In the long run, each case is different and should be treated individually, Beery says. And, the help a landlord provides should be a temporary solution. "It is very difficult to raise rents back up to market if the tenant has gotten used to a certain rate for two or three years." And generally, it's better to retain a healthy tenant at market rate who is in an industry with promise of future growth, he adds.

The Rent Reduction Route

"So far this year, we have half the amount of leases we had last year, going from about 400,000 sf to 200,000 sf," says **Lenore Reynolds, CCIM, vice president of leasing for retail brokerage Bruce Strumpf, in Clearwater, Fla.** Reynolds and her colleagues decided to do a considerable amount of short-term rent reductions, cutting rent by 25 percent, with plans to re-evaluate after three months.

"We are approaching it on a case-by-case basis. There is no blanket policy for existing tenants," Reynolds explains. "However, current tenants tend to get more consideration than new ones," she adds. For prospective tenants, Reynolds may offer substantial rent reductions for the first six to 12 months, depending on the deal's economics. It also depends on whether or not the landlord has to provide any TIs prior to occupancy, she says.

"The rent quote doesn't mean anything anymore. And, each deal is more preposterous than the next," Reynolds says. For instance, Reynolds dropped

the rent from \$16 psf to \$14 psf to lock in a small regional tenant in Orlando, Fla., that specializes in rent-to-own products. The deal closed at \$11 psf. Plus, "The tenant wanted \$22,000 in tenant improvements, which included putting in a roll-up backdoor, upgrading the bathrooms to be handicap accessible, and taking down a wall." In another example, a national retail tenant who leases more than 500,000 sf in a Tampa, Fla., power center asked for a 25 percent base reduction. "We almost fell over," she says.

But it's important to stay competitive to retain tenants, Reynolds notes. "Our landlords are contributing by advertising in local periodicals for their tenants," she says. "They are getting very creative and stepping up to the plate because they don't want to lose tenants." In addition, Reynolds' company is giving landlords more money for marketing and direct-mail campaigns. "E-blast campaigns also help us stay ahead of the competition as well as getting back to basics," Reynolds says. "We are still doing cold calls even though we get over 100 calls a month from prospective tenants. We also stay in constant contact with tenant representative brokers and retail brokers."

A New Look on Leasing

"In late November 2008, I took over the leasing for an 80,000-sf office building on Maui," says **Cynthia R. Greenwell, CCIM, senior vice president of sales and leasing for Kean Properties in Kihei, Hawaii.** The building was about 85 percent occupied and the vacant space was a large office that had never been built out due to its location under a parking garage. Physical restrictions also made it undesirable to prospective tenants, she explains.

The remaining offices were 10 small executive suites, two small offices, and one 2,470-sf office. "Without new tenants knocking on my door, I decided to do whatever it took to keep the existing tenants."

"After studying rent rolls, I noticed that several tenants whose lease terms were up had been allowed to go month-to-month while other tenants whose terms were up had renewals in limbo," Greenwell says. For these tenants, "I offered a rent reduction based on the length of lease they were willing to sign." Basically, the longer the lease term, the lower the base rent, she says. Greenwell also offered her tenants other options such as holding the base rent at the prior year's level, free parking, and TI money for new paint or carpet, she says. "Since, for the most part, the tenants were happy with their offices, it was just a matter of determining what their concerns were and then addressing those needs." And even though some smaller tenants elected to keep their leases month to month, which is less than ideal for landlords, allowing this instead of losing a tenant was a no-brainer, she adds.

While the lease length already was determined for tenants with lease renewals, "we still worked with beginning base rent, annual increase reductions, and offering the same incentives as our month-to-month tenants." For lease renewal tenants especially, "I always try to present these options in terms of effective base rent to show tenants the value of incentives," Greenwell says.

Now, Greenwell is looking at tenants whose leases expire in 2010, but don't have an option to renew. "I am contacting them in the hopes that I can convince them that renewing now, while it's still a tenants' market, is a wise move. They can negotiate a better deal now instead of when their lease expires," she says. For instance, she has started the negotiation process with a 5,000-sf national financial services tenant whose lease is up at year-end. "First, I plan to just get a feel for how they are doing in this market - if the office is buzzing or not," Greenwell explains.

"I usually don't start out by offering more incentives than necessary because you can't take it back if you find out the company is doing well and didn't actually need them." It's important to remember that it's "easy for both tenants and landlords to panic and rush to the table either demanding or offering too much. After that, it becomes more difficult to backtrack."